VZCZCXYZ0005
RR RUEHWEB

DE RUEHSK #0364/01 0900659
ZNY CCCCC ZZH
R 310659Z MAR 06
FM AMEMBASSY MINSK
TO RUEHC/SECSTATE WASHDC 4160
INFO RUEHKV/AMEMBASSY KIEV 3228
RUEHMO/AMEMBASSY MOSCOW 3407
RUEHRA/AMEMBASSY RIGA 1635
RUEHVL/AMEMBASSY VILNIUS 3630
RUEHWR/AMEMBASSY WARSAW 3286
RUEHBS/USEU BRUSSELS
RUEHVEN/USMISSION USOSCE 1056
RHMFISS/HQ USEUCOM VAIHINGEN GE
RUFOADA/JAC MOLESWORTH RAF MOLESWORTH UK

C O N F I D E N T I A L MINSK 000364

SIPDIS

SIPDIS

E.O. 12958: DECL: 02/15/2016
TAGS: ECON EPET PREL ENRG ETRD BO
SUBJECT: USD 2.5 BILLION IN RUSSIAN SUBSIDIES IN 2005

Classified By: Classified by Ambassador George Krol for Reasons 1.4(B,D
)

¶1. (U) Summary: According to the best numbers available, Russia provided approximately USD 2.531 billion in subsidies, mostly energy, to Belarus in 2005. Of that, USD 1.236 billion came from the sale of discounted natural gas, USD 1.149 billion from the sale of discounted crude oil, and USD 146 million in the form of a governmental loan. This amounts to 9.5% of GDP (just under USD 27 billion in 2005, according to GOB estimates). In addition to this total, the GOB demands that any company supplying crude oil to the two Belarusian refineries must sell a set portion of the refined product to Belarusian enterprises, many of whom are state owned, at discounted prices. End summary.

¶2. (C) Estimates of Russian subsidies to the GOB vary greatly. Economic analyst and former head of the National Bank of Belarus Stanislav Bogdankevich recently told the Russian press that Belarus receives more than USD 4 billion a year from Moscow in subsidies. Citing a report by Moscow's Trust Investment Bank, Bogdankevich claimed the GOB earns nearly USD 3 billion from the resale of under-priced Russian crude oil. In contrast, Valery Dashkevich, an economist with Minsk's BelGazpromBank, told Econoff that Russian subsidies are closer to USD 1.1 to 1.3 billion per year.

Natural Gas, USD 1.236 billion

¶3. (U) The largest source of Russian subsidies is the sale of natural gas to Belarus. The GOB buys natural gas solely from Russia's Gazprom, paying a steeply discounted price of USD 46.68 per thousand cubic meters (tcm). In contrast, Lithuania pays USD 120/tcm and Ukraine USD 230/tcm (to Gazprom, although its average cost is lower after Turkmen gas is added). (Note: these countries are roughly the same distance from Russia's gas fields as is Belarus.)

¶4. (U) Compared to Lithuania, Belarus pays USD 73.32 less per tcm. Since Belarus consumed 20.12 billion cubic meters (bcm) of Russian gas in 2005, that subsidy totals roughly USD 1.475 billion a year.

Minus Discounted Transit

¶5. (U) One of the justifications for paying less for gas is that Belarus also charges less than Ukraine does for gas transit. Using 2006 rates for comparison, Ukraine charges USD 1.60/tcm per 100 kilometers. Belarus has two pipeline systems, the Gazprom-owned Yamal-Europa (YE) pipeline and the GOB-owned Beltransgaz pipeline network. The GOB charges USD 0.46/tcm/100 km on YE and USD 0.75/tcm/100km through Beltransgaz. (Note: For calculating charges, we assume both pipelines are 575 kilometers long (the length of YE.) Beltransgaz's length varies depending on destination country. Sources differ on whether the GOB treats all transit through Beltransgaz as if it were 575 km or whether it measures actual pipeline length.)

¶6. (U) In 2005 Belarus transited 24 bcm of gas through YE, earning USD 63.48 million, and 16.8 bcm through Beltransgaz's network, earning USD 72.45 million, for a total of USD 135.93 million earned through transiting Russian gas exports to Europe. (Note: Unless gas transit increases, Belarus will earn less transit money for 2006. In 2005 Gazprom added compressor stations to YE, boosting its throughput. In the first two months of 2006 transit volumes through YE are up 57.8% on the year, and down through Beltransgaz by 16.4% as Gazprom shifts gas into the cheaper network.)

¶7. (U) If the GOB charged the same rate as does Ukraine for transit (USD 1.60/tcm/100 km in 2006), it would have earned an additional USD 239.43 million. Therefore, taking this difference in transit prices into account, the GOB's total gas subsidy from Russia drops to an annual USD 1.236 billion.

-- ----------
Oil: The (Relatively) Simple Picture, USD 1.149 billion
-- ----------

¶8. (U) According to GOB statistics, in 2005 Belarus imported 19.232 million tons of crude oil from Russia at an average cost for the year of USD 218 per ton. (Note: assuming 7.3 barrels per ton, this comes to USD 29.86/barrel.) The Moscow Times reported that the 2005 average price for Russian Urals blend was USD 50.50/barrel, or USD 368.65 per ton.

¶9. (U) According to GOB statistics, Belarus' two refineries owned 7.549 million tons of this crude themselves (Mozyr 3.64 million, Novopolotsk 3.909 million). (Note: While the GOB owns 99.8% of the Naftan refinery in Novopolotsk, it only owns 55% of the Mozyr refinery (43% is owned outright, and 12% is owned by the MNPZ association, which the GOB took over through the Golden Share in 2005). Russia's Slavneft owns another 42.5% of the Mozyr refinery. Therefore, we can only consider 2.002 million tons of the Mozyr-owned crude to be the property of Belarusian interests.)

¶10. (U) In addition, Belarusian state-owned companies delivered additional crude supplies to the refineries. Belorusneft supplied 1.511 million tons (of which 441,000 tons was domestically produced, leaving 1.07 million tons purchased from Russia), Belneftekhim supplied 527,000 tons of Russian crude, and the Gomel-based oil transport company Druzhba supplied another 40,000 tons. These companies contributed a total of 1.637 million tons of additional Belarusian-owned Russian crude. The Belarusian company Triple is also believed to purchase discounted Russian crude, but no data was available.

¶11. (U) The GOB therefore owned 7.629 million tons of the Russian crude that it imported. Purchased at a per ton discount of USD 150.65, this shows Russia subsidized Belarusian crude oil consumption and re-export of refined crude to a total of USD 1.15 billion.

¶12. (U) (Note: Belarus regularly imports far more crude than it can consume domestically. In 2005, Belarus refined and re-exported 13.487 million tons of Russian crude (495,000 tons to CIS countries and 12.992 million tons to non-CIS states). In recent years it was profitable for Russian oil companies to ship crude to Belarus, where it was refined,

before exporting it westwards. Russia did not charge oil export duties on crude going to Belarus, and Belarusian duties were usually lower than Russian ones, allowing Russian companies to pay lower export duties by shipping through Belarus. However, in early 2006 the GOB finally matched its oil export duties to Russia's, eliminating this loophole.)

Oil: The More Complex Picture

Crude Suppliers Must Sell Refined Products at a Discount

¶13. (U) In addition to receiving Russian crude at a discount, the GOB also demands that all companies that supply crude oil to Belarus' two refineries sell a portion of the refined product inside Belarus at discounted rates, which are set by the GOB. The quantities change, but as of December the GOB insisted that any company supplying crude oil to the Naftan refinery:

--Sell all paraxylene produced to the GOB-owned concern Belneftekhim;
--Sell all benzene produced to Khimvolokno, a Grodno-based joint venture (partially state owned) that produces artificial fibers;
--For every ton of crude supplied, the company must sell on the Belarusian market 80 kilograms of Normal-80 gasoline, 3 kg of fuel oil, 2 kg of A-92 gasoline, and 114 kg of diesel fuel (the only exception is when the crude is delivered by rail, then the supplier must sell 25 kg of Normal-80 gasoline rather than 80 kg);
--For every ton of crude the supplying company must also sell 5 kg of oil products to Belarusian agricultural companies for below market value.

¶14. (U) The GOB demanded that any company supplying crude to the Mozyr refinery:

--Sell on the Belarusian market 34 kg of Normal-80 gasoline, 69 kg of fuel oil, 46 kg of A-92 gasoline, and 30 kg of diesel fuel;
--For every ton of crude the supplying company must also sell 5 kg of oil products to Belarusian agricultural companies for below market value.

¶15. (SBU) Post was not able to determine what rates the GOB sets for the sale of the above products, as this information is classified. However, the rates are low enough that gasoline remains cheaper in Belarus than in most of the rest of Europe, and these rates do not fluctuate with the international price of crude. For instance, A-92 gasoline has remained at BYR 1400 (USD 0.65) per liter for at least six months, with absolutely no fluctuation after Hurricane Katrina. Post cannot estimate the value of this additional energy subsidy for the GOB.

Oil Sold Through Shell Companies

¶16. (C) Independent economist Jaroslav Romanchuk and energy specialist Elena Rakova of the Institute for Privatization and Management separately told Econoff that the situation with oil subsidies is much more muddled. Russian oil companies are ostensibly private, but still sell crude to Belarus at up to a 2/3rds discount. Romanchuk and Rakova both explained that Russian companies sell to Belarus' refineries, which process the crude and ship it to the Belarusian border, where it is again sold to a variety of Russian and Belarusian front companies in Europe before being sold again in reputable markets, such as the London Petroleum Exchange. This set of front companies allows various people in Russia and Belarus to take extra commissions and cuts of the profits. While the numbers above are accurate, it is unknown who exactly profits from the import and re-export of

cheap Russian oil. It is probably that a sizeable portion of this money is going into private hands (Belarusians well-connected with the Lukashe
nko regime), as well as to some Russians, rather than into any GOB accounts.

¶17. (C) Romanchuk said that a similarly muddled series of front companies and transactions exists regarding Belarusian imports of unprocessed metals.

Loan, USD 146 million

¶18. (U) While not exactly a subsidy, Moscow is lending money to the Lukashenko regime. To offset a modest increase in natural gas prices in 2004, the GOR provided Belarus with a loan of USD 175 million. Moscow again provided Minsk with a USD 146 million loan in December 2005. Under the terms of the loan, the GOB will have to repay the loan after five years. Interest is calculated at the Libor three-month rate (currently just under 5%) plus 0.75%.

Comment

¶19. (SBU) USD 2.5 billion in Russian energy subsidies, plus whatever the GOB makes on the forced sale of refined oil products at discounted prices, makes up close to 10% of GDP. This has been a tremendous boost to the Belarusian economy and has been a great aid to largely inefficient Belarusian industry. Even while receiving heavily subsidized gas and oil, energy accounts for on average 9.8% of the production cost of Belarusian goods (according to the World Bank). If Russia were to raise the price for gas, as many believe will happen in the next few months, the GOB would be faced with both the difficulty of higher energy costs, as well as the decreasing competitiveness of Belarusian industry.
Krol